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C O N F I D E N T I A L SECTION 01 OF 04 BUDAPEST 001058

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SUBJECT: SPECIAL ENVOY GRAY TALKS PIPELINES, CLIMATE POLICY  
IN BUDAPEST

REF: A. BUDAPEST 1021  
[B. BRUSSELS 1686](#)

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Classified By: P/E Counselor Eric Gaudiosi, reasons 1.4 (b, d)

¶1. (C) SUMMARY: During his two-day trip to Budapest to take part in an energy conference, Special Envoy Gray held a series of meetings with regional energy officials and experts. These conversations revealed that despite recent Russian diplomatic and financial setbacks, Gazprom and its partners are moving forward on the South Stream pipeline feasibility study while Moscow is apparently working to influence the outcome of the Southern Corridor pipeline project in Turkey and the Balkans. Hungary, Bulgaria, and the Czech Republic are hoping to keep a spotlight on Central European energy security and the Southern Corridor as they host a series of energy summits in 2009. Ukraine is making a bid to retain its role in European energy transit following the construction of planned pipelines that circumvent it. On climate policy, Hungary indicated it would not agree to the French proposal to change the base year for emission reduction requirements from 1990 to 2005 without coordination, but that it might be open to a compromise base year sometime between 1990 and 2005. Hungary, like Poland, wants to take the lead in coordinating a policy with fellow new EU members. END SUMMARY.

¶2. (SBU) US Special Envoy for Eurasian Energy Boyden Gray visited Budapest October 28-29 to take part in the 3rd Energy Forum, a conference jointly organized by Hungary,s Constellation Energy Institute and Poland,s Eastern Institute and held under the patronage of President Solyom. On the margins of the conference, Special Envoy Gray met with Peter Poptchev, Bulgaria,s Ambassador for Energy Security and Climate Change and Coordinator for Nabucco, Bohdan Sokolovskyj, the Ukrainian Presidential Representative for International Energy Policy, and Zeyno Baran, a Eurasian energy expert from the Hudson Institute. Special Envoy Gray also met with Hungary,s Ambassador-at-Large for Nabucco, Mihaly Bayer, at his office, and held a breakfast meeting

with Senior State Secretary Dr. Lajos Olah of the Ministry of Environment and Water, and Tibor Farago, the Ministry's Head of Strategic Planning, who represents Hungary at EU climate change meetings.

#### SOUTH STREAM: PROGRESSES, AT LEAST ON PAPER

¶3. (SBU) Much of the conversation with Poptchev and Bayer centered on Russia and the state of play with South Stream. Both see Russia in a weakened position following the Georgia conflict and as a result of the financial crisis. Poptchev posited that Russia is "unsure of itself" and "sorry for its actions in Georgia." Bayer believes Russia still would like to integrate into Western institutions, albeit on its own terms, but the loss of confidence by the West in Russia, post-Georgia, and the impact of the financial crisis and lower energy prices on its hard currency reserves suggest it lacks the means to bend the West to its will.

¶4. (C) Poptchev and Bayer both made it a point to emphasize that Bulgaria and Hungary are merely transit states for South Stream, which they described as a diversification project for Italy. Special Envoy Gray responded that based on recent conversations with ENI management, from the Italian company's perspective, South Stream has not moved beyond an agreement with Gazprom for a two-year feasibility study. Planning for the project, however, appears to be proceeding in both countries under a veil of secrecy. Poptchev reported that "they are working day and night" on the Bulgarian feasibility study, but that information is being compartmentalized with Bulgargaz, Moscow representative taking the lead while the Sofia office is kept in the dark. Bayer's statements to Gray and to Ambassador Foley in a

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separate meeting on October 27, that Hungary's progress on South Stream is facing delays, suggest that he is similarly out of the loop in light of Hungarian National Security advisor Banai's assertion that an announcement could come any day (see reftel A).

#### RUSSIAN ROLE IN BALKANS, NABUCCO?

¶5. (C) It eventually became clear that Poptchev had requested the meeting with Gray to put forward a proposal that Russia be included as an economic development partner in the West Balkan region. (Note: It was not clear if this proposal was Poptchev's own idea, from the Bulgarian government, or from the Russian side. In his conference presentation, Poptchev remarked that Bulgaria considers South Stream part of its West Balkan neighborhood policy. End note.) He contrasted the EU's lack of significant development assistance to the region and Nabucco's planned bypassing of these countries with the assertion that South Stream would provide gas to them and might offer a way for Russia to play a positive role. He suggested that the US elections and the financial crisis might offer everyone a chance to take a step back from energy geopolitics to consider such a role for Russia, but he also said he favors forward progress on Nabucco whether Russia likes it or not.

¶6. (C) After remarking that even Gazprom officials in Sofia expect Nabucco to be eventually completed, Poptchev suggested that linking Nabucco with the Blue Stream pipeline in Turkey and using it to transport Russian as well as Caspian gas might help make the project more viable. (Note. Once again, it was not clear if this was Poptchev's own proposal, the Bulgarian government's or Russia's. End Note.) When asked, Poptchev was not sure if this would also mean Gazprom membership in the Nabucco Consortium and part ownership of the pipeline.

#### NABUCCO NEEDS GOOD NEWS

¶7. (SBU) Special Envoy Gray discussed with Bayer and Poptchev the ambitious schedule of upcoming Central European

energy conferences, beginning with the Nabucco Summit Budapest plans to host in January, followed by a more broadly-focused Energy Summit, to include Russian representation, in Sofia in April and an EU-Trans Caspian Summit the Czechs are planning for the latter half of their EU presidency, which will run from January-June 2009. Special Envoy Gray stressed the importance of coordinating these three events to ensure the maximum impact, particularly given the Czech EU presidency, and to avoid redundancy.

Poptchev said Sofia has reached out to Prague and Budapest, but that the Czechs were reluctant to include the Budapest and Sofia events on the official docket for their presidency.

Bayer told Ambassador Foley in their meeting on October 27 that he will soon travel to Sofia to iron out objectives for the first two conferences, but that neither Budapest nor Sofia had any details on the Czech summit. Similarly, Hungarian officials have pressed us for more details regarding an upcoming energy conference in Baku, expressing their desire to coordinate with Azeri officials and indicating that PM Gyurcsany may attend. Bayer and Poptchev both requested US engagement in encouraging high-level attendance by conference participants and in helping to facilitate coordination among the capitals to help ensure that the upcoming conference are complementary.

¶8. (SBU) Bayer said he hopes preparations for the Nabucco Summit might stimulate progress toward completion of an Intergovernmental Agreement (IGA) among the Nabucco countries. Additionally, the Summit might provide a framework for harmonizing an eventual IGA in accordance with Turkey's insistence on a series of Host Government Agreements (HGAs) with the companies forming the Nabucco

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Consortium. He does not expect the IGA to be ready to be signed by the Summit, but believes that having politicians, energy companies and investors at the same table in Budapest could give lift to the process. He described a recent meeting in Budapest of representatives from the five EU Nabucco transit states to discuss the relationship between the IGA and HGAs. The EU countries were not opposed to the idea of an HGA, but all considered an IGA more attainable in the near-term and agreed that, given the need for some good news on Nabucco after the Georgia invasion, efforts should remain primarily focused on successfully adopting an IGA.

¶9. (SBU) Poptchev and Bayer both mentioned unresolved issues surrounding Turkish transit of Nabucco gas as key impediments to concluding a deal. At a recent EU meeting on Nabucco, Poptchev proposed opening the EU energy chapter for Turkey as an inducement to Ankara, but Cyprus blocked it. Bayer believes it to be a good sign, however, that Turkish Prime Minister Erdogan is planning to attend the Budapest summit.

¶10. (SBU) Despite the boost Nabucco receives from German energy giant RWE's addition to the Nabucco Consortium, Bayer does not expect the project to benefit from German political support as Berlin wants to avoid any indication that it is favoring one infrastructure project over another. He added that Chancellor Merkel is further constrained by her current bid for re-election. As such, he does not expect her to accept the invitation to attend the Budapest summit in January.

#### UKRAINE HOPES FOR FUTURE TRANSIT ROLE

¶11. (SBU) Ukrainian Presidential Representative for International Energy Policy Bohdan Sokolovskyj requested a meeting with Special Envoy Gray to pass on a proposal for a Caspian/Black Sea/Baltic Energy Transit Space. Kiev plans to present the proposal at the November 13-14 Energy Summit in Baku and would like the US to engage on its behalf with the EU. Several EU members are apparently awaiting signals from Brussels, while Baku is interested but wants to see favorable reactions from Polish and Baltic partners before it proceeds. Sokolovskyj reported initial indications of interest from

the Lithuanian government and from Polish President Kaczynski, although the Polish government remains noncommittal. Special Envoy Gray offered to take the issue up with Warsaw when he visits in December.

¶12. (SBU) Sokolovskyj also wanted to sound out the Special Envoy,s views on White Stream, a proposed pipeline that would carry Caspian gas to EU customers via the Black Sea and Ukraine. Special Envoy Gray said it was worth considering, particularly because it would create competition for Turkey, which continues to play hardball on Nabucco.

#### FROM RUSSIA WITH HATRED

¶13. (C) Zeyno Baran, in a pull-aside meeting at the conference, told Special Envoy Gray the Russians are making a full-court press to drive a wedge between Turkey and the EU, particularly with regard to Nabucco. She surmised that the Russians are taking advantage of US focus on our elections and political transition to secure maximum gains. Her Turkish contacts tell her that Russia is again pushing for a second Blue Stream pipeline and demanding that Russian gas be included in any Southern Corridor pipeline configuration. A proposal by Moscow for a Russia-Turkey-Iran trilateral agreement whereby Iranian gas would be developed for use in Iran and Turkey is apparently gaining a following among those in Turkey who are opposed to a deal with Azerbaijan. She suggested that improved prospects for Iraqi gas transiting Turkey might undercut Russian moves and help keep Turkey focused on Nabucco.

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¶14. (C) Baran also related a personal account that is perhaps indicative of this more aggressive Russian posture. At the dinner reception following the first day of the conference, a Russian participant named Vladimir Sizov, Director of the Center for Military-Strategic Studies, Institute for US and Canada Studies, interrupted a conversation she was having to berate her for her presentation on energy security, which, he claimed, was tantamount to a "new US military doctrine." According to Sizov (and numerous other Russian participants at the conference), the US is trying to start a new Cold War and is using the issue of energy security to make Europe more confrontational toward Russia. (Note: Econoff noted a large, vocal Russian presence at the conference from a variety of private sector, governmental, and non-governmental institutions, generally sharing the same, if sometimes less forcefully stated, message. End note.) He then personalized his critique of Baran,s presentation, saying "We know who you are. We hate you. We are following you."

#### HUNGARY SEEKING FURTHER COORDINATION ON BASE YEAR EMISSIONS

¶15. (SBU) At his meeting with Messrs. Olah and Farago from the Ministry of Environment, Special Envoy Gray discussed linkages between energy and climate policies and asked the Hungarians their views on the Polish opposition to the French initiative to change the EU,s base year for calculating emissions reductions to 2005 (ref B). Olah was doubtful that a deal would be reached at the next UN Conference on Climate Change scheduled for December 2008 in Poznan. He indicated that Budapest could not accept the French proposal without coordination, and that Hungary, like Poland, wants to be a coordinator of the newly-acceded EU states. According to Olah, Hungary has many arguments for keeping 1990 as the base year but is open o considering setting the base year somewhere between 1990 and 2005. Farago underlined the importance of agreeing in Poznan on specific next steps, noting that there would be no deal without the US and that there is a place for China and India as well.

¶16. (C) COMMENT: If Ms. Baran is correct in her view that Moscow is aggressively countering US policy on European and Eurasian energy in hopes of catching the US off-balance

during our election cycle, then Nabucco and/or other Southern Corridor projects that would bring Caspian gas to Europe through non-Russian controlled pipelines could definitely use some offsetting good news. A successful series of summits, beginning with the one in Budapest in January, could give Nabucco a needed boost, provided they are properly coordinated among the hosts and identify meaningful but achievable objectives. Post will remain engaged with GOH and Ambassador Bayer to that end. We remain concerned, however, that any such good news might be trumped by the next announcement of progress on the Hungarian segment of South Stream, which we believe to be inevitable... and potentially timed to undermine the Nabucco Summit itself. END COMMENT.

¶17. (U) Special Envoy Gray cleared this cable.  
Foley